No. 83-653

In the Supreme Court of the United States

October Term, 1983

LEATHERBY INSURANCE COMPANY, a/k/a WESTERN EMPLOYERS INSURANCE COMPANY,

Petitioner,

vs.

MERIT INSURANCE COMPANY,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

BRIEF IN OPPOSITION

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QUESTIONS PRESENTED FOR REVIEW*

1. Whether the court of appeals correctly held that a moving party is not entitled to relief from a judgment under Fed.R.Civ.P. 60(b), based on "newly discovered evidence," when the moving party has shown neither: (a) that its officers and directors, as opposed to its trial attorneys, were ever actually unaware of the "newly discovered evidence," nor (b) that such evidence, even if newly discovered, could not have been discovered earlier through the exercise of due diligence.

2. Whether the court of appeals correctly held that an arbitrator's failure to disclose a stale, limited, and non-pecuniary association with an officer of one of the parties, which terminated 14 years before the commencement of the arbitration, does not constitute "evident partiality" warranting vacation of a unanimous arbitration award.

3. Whether the court of appeals erred in rejecting "findings of fact" which either were wholly unsupported by the evidence in the record or were ultimate conclusions of law.

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* Respondent Merit Insurance Company is a wholly-owned subsidiary of Merit Financial Corporation, which is privately held.

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BRIEF IN OPPOSITION

STATEMENT OF THE CASE

A. The Procedural Background

In December 1980, Merit Insurance Company ("Merit") commenced this action in the district court under 9 U.S.C. §9 to confirm a $10.675 million arbitration award entered by a panel of three neutral arbitrators, who unanimously found that Leatherby Insurance Company ("Leatherby")

had defrauded Merit in that amount (Pet. App. 2).[1] Leatherby moved to vacate the award under 9 U.S.C. §10 (App. 1, 7). After the district court had confirmed the award (App. 1-22) and denied Leatherby's subsequent motion under Fed.R.Civ.P. 60(b) for relief from the judgment (O.R. Item 70), Leatherby appealed (Pet. App. 3).[2]

In May 1982, while that appeal was pending, Leatherby filed a second Rule 60(b) motion in the district court, alleging that it had recently discovered that one of the arbitrators, Jack F. Clifford, and Jerome H. Stern, the president of Merit, both had been employed by Cosmopolitan Insurance Company ("CIC"), a wholly unrelated and now defunct insurance company, for a period of about two years, ending more than 14 years before the commencement of the arbitration.[3] Leatherby claimed that Mr.

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[1] The following abbreviations will be used in referring to the record:

"Pet. App." for the appendix annexed to the petition;

"App." for the appendix annexed to this brief;

"O.R. Item" for original record materials;

"Leatherby C.A. Br." for Leatherby's brief in the court of appeals;

"C.A. Pet.R." for Leatherby's petition for rehearing in the court of appeals;

"S.A." for Merit's supplemental appendix in the court of appeals; and

"Tr." for the transcript of the evidentiary hearing on Leatherby's second Rule 60(b) motion.

[2] This appeal was docketed in the court of appeals as No. 81-3053.

[3] The court of appeals denied Leatherby's motion to stay oral argument in No. 81-3053, which motion was based on the same grounds asserted in Leatherby's second Rule 60(b) motion. Several months after the court of appeals heard oral argument in No. 81-3053, it granted Leatherby's motion to dismiss that appeal.

Clifford's failure to disclose this fact constituted "evident partiality" warranting vacation of the award under 9 U.S.C. §10(b). Following a hearing, the district court granted Leatherby's motion, vacated the judgment confirming the award, and vacated the arbitration award (Pet. App. 40).

On Merit's appeal from that judgment, the court of appeals, in a unanimous decision, reversed and remanded, instructing the district court to reinstate the judgment confirming the award (Pet. App. 1-18). Leatherby's petition for rehearing and suggestion of rehearing en banc were subsequently denied, with no judge in regular active service requesting a vote on the suggestion of rehearing en banc (Pet. App. 43).

B. The Substantive Dispute and the Arbitration

The history of this protracted litigation begins in October 1972, when Leatherby and Merit executed a reinsurance and assumption agreement. In that agreement, Merit undertook to reinsure all claims that could be made against Leatherby through its retrospective agent, General Auto Placement, Inc. ("GAP") (App. 2). As the arbitrators found and the district court noted in its original opinion confirming the arbitration award (App. 2-5), Leatherby had failed to disclose several material facts with respect to the reinsurance transaction and concealed "secret" cash reserves, thereby fraudulently inducing Merit to enter into the agreement.

In 1976, after discovering this fraud, Merit brought suit against Leatherby and certain other parties in the United States District Court for the Northern District of Illinois. Leatherby, based on an arbitration clause in the reinsur-

ance agreement, moved successfully to compel arbitration.[4] The parties subsequently selected as arbitrators three prominent Chicago lawyers (including a past president of the Chicago Bar Association and a former Director of the Illinois Department of Insurance), all of whom were experienced in insurance matters (App. 1). The panel heard live or deposition testimony from more than 25 witnesses in an arbitration that spanned three years and 120 sessions, and which eventually produced a transcript in excess of 16,000 pages (App. 1-2). In December 1980, the panel unanimously awarded Merit damages in the amount of $10.675 million, which was approximately one-third of the total amount sought (*see* App. 5-6).

C. The Proceedings to Confirm the Award

In December 1980, Merit petitioned in the United States District Court for the Northern District of Illinois for confirmation of the award under 9 U.S.C. §9. Leatherby tenaciously opposed confirmation. Among other things, Leatherby claimed that the arbitration panel was biased, but that claim was based solely on Leatherby's disagreement with certain evidentiary rulings and on a single comment made by Arbitrator John Bolton during the three-year arbitration (App. 18-20).[5]

The district court exhaustively reviewed the entire arbitration record and confirmed the award on November 19, 1981. In a comprehensive memorandum opinion, the dis-

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[4] *See Merit Ins. Co.* v. *Leatherby Ins. Co.*, 581 F.2d 137 (7th Cir. 1978). *See also Merit Ins. Co.* v. *Colao*, 603 F.2d 654 (7th Cir. 1979), *cert. denied*, 445 U.S. 929 (1980).

[5] Leatherby also moved to vacate the arbitration award in state and federal courts in New Jersey, but those actions were dismissed for want of jurisdiction (O.R. Item 85 at 1-14).

trict court found Leatherby's allegations of bias to be "distinctly hollow" (App. 20) and rejected each of Leatherby's other contentions as well (App. 9-18). Leatherby then moved under Fed.R.Civ.P. 60(b) for relief from the judgment, claiming that the arbitrators had not sufficiently explained the reasons for their award (O.R. Item 62). That motion was promptly denied (O.R. Item 70).

Leatherby appealed from the judgment confirming the award and the order denying relief under Rule 60(b). On appeal, Leatherby challenged the amount of the damage award and made various technical objections to the conduct of the arbitration, but it neither challenged the arbitrators' finding of liability nor pursued its bias claim.[6]

On May 12, 1982, after its appeal had been fully briefed and set for oral argument, Leatherby filed a second Rule 60(b) motion in the district court, this time claiming that it had "recently discovered" that Arbitrator Jack F. Clifford and Mr. Jerome Stern, the president of Merit, both had been employees of CIC for a period of about two years, ending some 14 years before the arbitration (O.R. Item 94).[7] Leatherby claimed that Mr. Clifford's

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[6] *See, e.g.*, No. 81-3053 (7th Cir.), Leatherby Br. at vi (filed March 15, 1982).

[7] Initially, Leatherby sought vacation on the additional ground that Mr. Clifford had failed to disclose that Gerald Rotheiser, one of Merit's several vice-presidents, had also worked at CIC during the same period. It was clear from the evidentiary hearing, however, that Mr. Rotheiser and Mr. Clifford never had any even arguably significant contact, professional or social, before, during, or since the period of their common employment. The district court did not base its ruling on Leatherby's argument with respect to Mr. Rotheiser, and Leatherby did not renew that argument in the court of appeals. *See* Pet. App. 4.

failure to disclose this fact constituted "evident partiality" warranting vacation of the award under 9 U.S.C. §10(b).

D. The District Court Hearing and Decision on Leatherby's Second Rule 60(b) Motion

The district court conducted an evidentiary hearing on Leatherby's motion. The evidence showed that Robert Jacobson, CIC's chairman, hired Mr. Clifford in late 1960 to be vice-president in charge of CIC's claims department (Pet. App. 3). Mr. Clifford, who then had more than 10 years' experience in handling claims for a national insurance carrier, was induced to join CIC by Mr. Jacobson's promise of virtual autonomy (*see* Pet. App. 3). Mr. Stern, who was already employed at CIC, was promoted from Treasurer to Executive Vice President about the same time (Pet. App. 3). As head of the claims department, Mr. Clifford technically reported to Mr. Stern, but the latter was principally engaged in unrelated facets of CIC's business, such as the acquisition and management of related companies, and he had had no experience at that time in claims matters (Pet. App. 3-4).

Over the entire two-year period of their common employment, the contacts between the two men were extremely limited. As the district court specifically found (Pet. App. 28), Mr. Stern and Mr. Clifford attended about 10 meetings together during this period, Mr. Clifford reported to Mr. Stern on only a handful of specific claims, and Mr. Stern once required Mr. Clifford, along with other employees, to take a polygraph examination. In addition, Mr. Clifford was once assigned to evaluate the claim reserves of a company CIC proposed to acquire, but the uncontroverted evidence was that Mr. Clifford was neither assigned this task by Mr. Stern nor reported the results

to him.[8] The evidence further established that Mr. Stern and Mr. Clifford never had any social contact whatsoever, and never even had a business lunch together, during or after the period of their common employment (Pet. App. 29). Mr. Stern left CIC in February 1963 (Pet. App. 21), and though both men remained active in insurance matters in the City of Chicago, they had no contact of any kind, professional or social, during the 14 years preceding the arbitration (*see* Pet. App. 4).[9]

Although Leatherby's Rule 60(b) motion was premised upon its allegedly "recent discovery" of Mr. Clifford's prior association with Mr. Stern, Leatherby offered no evidence, not even by affidavit, to establish that its officers or directors, as distinguished from its trial attorneys, were actually unaware of this association, either at the time Mr. Clifford was selected to serve as an arbitrator or, indeed, at any time prior to filing the second Rule 60(b) motion (*see* Pet. App. 16). At the hearing, Leatherby elicited testimony from its trial lawyers and expert witness to show that *they* were unaware of Mr. Clifford's employment at CIC (Tr. 424-25, 456-57, 479), but Leatherby conspicuously avoided calling any of its officers

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[8] The district court's finding (Pet. App. 28) that Mr. Stern had assigned this task to Mr. Clifford was plainly mistaken, because there was no evidence in the record to support it. *See, e.g.,* Tr. 203 The district court made no finding as to whether Mr. Clifford reported on this matter to Mr. Stern, but the evidence is uncontroverted that he did not. *See, e.g.,* Tr. 203-04.

[9] The opinion of the court of appeals apparently contains a typographical error in that it states (Pet. App. 4) that "Clifford and Stern . . . spoke to each other on the phone on one or two occasions but these contacts were of no significance . . . ." The transcript shows that the court's reference to Mr. Stern should be to Mr. Rotheiser. *See* Tr. 403-04.

or directors to establish Leatherby's lack of knowledge. Indeed, Leatherby affirmatively thwarted Merit's attempt to develop evidence on this point by invoking the work product doctrine to prevent Leatherby's trial attorneys from testifying as to how they learned of Mr. Clifford's prior association with Mr. Stern (*see* Tr. 459-61, 520). Similarly, Leatherby failed to establish that, even if it did not know of Mr. Clifford's past employment at CIC, it could not have discovered this fact by undertaking even the most rudimentary investigation into Mr. Clifford's background.[10] The court of appeals held that these omissions were fatal to Leatherby's claim (Pet. App. 16-17).

The district court nonetheless granted Leatherby's second Rule 60(b) motion. Although, as Leatherby points out

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[10] Mr. Stern's prior employment by CIC was a matter of record in this case (Tr. 481), and Mr. Clifford's was detailed in Martindale-Hubbell, not only for the years 1961 through 1963, when he was actually employed at CIC, but also for the years 1964 through 1966 (*see* O.R. Item 94 at Ex. D1-10). When the American Arbitration Association ("AAA") submitted Mr. Clifford's name to Donald Casey, Leatherby's principal trial attorney, as a potential arbitrator, the name was accompanied by only the following background information: "[D]eals with labor and probate; also Law Instructor, CPCU, Part IV Reinsurance" (Tr. 490-91). Mr. Casey did not ask the AAA for any further information. He checked Mr. Clifford's listings in the then-current editions of Martindale-Hubbell and Sullivan's law directories (Tr. 477-78), but did not check any previous editions of those publications, nor did he consult other readily available sources, such as biographical directories of insurance defense lawyers, with which he was admittedly familiar (Tr. 526-28). Mr. Casey made telephone inquiries of a few lawyers, who told him that Mr. Clifford was "a casualty defense attorney of long-standing [and] a man of integrity" (Tr. 478-79, 493-94), but Mr. Casey did not specifically ask any of them about Mr. Clifford's employment background or professional associations. This was the sum total of Mr. Casey's investigation of Mr. Clifford.

(Pet. 4-5), the district court found that "Leatherby and its attorneys and agents were unaware of Mr. Clifford's prior associations" (Pet. App. 24), there is no evidence whatsoever in the record to support that finding, and the court of appeals therefore properly rejected it. The district court also concluded that Mr. Clifford's association with Mr. Stern was not "trivial or insubstantial" during the early 1960s (Pet. App. 29), and that it "did not diminish by the passing of time" (Pet. App. 38). The record, however, is devoid of any evidence to support the latter finding because the uncontroverted evidence established that the two men had not even seen each other since 1963. The district court held that Mr. Clifford's failure to disclose his association with Mr. Stern constituted "evident partiality" under 9 U.S.C. §10(b).[11]

E. The Decision of the Court of Appeals

On Merit's appeal, the court of appeals reversed and remanded with instructions to reinstate the judgment confirming the award (Pet. App. 1-18). The court based its holding on three separate grounds. First, Leatherby had failed to meet the threshold requirements for extraordinary relief under Fed.R.Civ.P. 60(b). Relief under Rule 60(b), said the court, is an "extraordinary remedy," which may not be granted absent some showing of "a substantial danger of an unjust result" (Pet. App. 15-16). Leatherby failed to make that showing because it did not even estab-

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[11] Given the fact that Mr. Clifford's nondisclosure of his prior employment by CIC first occurred at least two years before the commencement of this arbitration (Pet. App. 4-5), his nondisclosure obviously had nothing to do with any desire to benefit Mr. Stern or Merit. Having given considerable attention to the question of Mr. Clifford's motivation, the district court was able to conclude only that Mr. Clifford may have wanted to distance himself from CIC, which had failed and created something of "an explosion in the industry" (Pet. App. 21).

lish that "its officers did not know of the relationship" which it claimed should have been disclosed (Pet. App. 16). If Leatherby's management was in fact aware of Mr. Clifford's long-past association with Mr. Stern, of course, no injustice possibly could have resulted from Mr. Clifford's failure to disclose it.[12]

Second, Mr. Clifford's failure to disclose his stale, limited and nonpecuniary association with Mr. Stern was insufficient to demonstrate "evident partiality" (Pet. App. 11-13).[13] The court reasoned that even if Mr. Clifford had been required by the AAA rules to disclose his prior association with Mr. Stern, that fact by itself would not require vacation of the award. Not every technical violation of the AAA rules will warrant vacation of an award on the statutory ground of "evident partiality." As the court of appeals noted (Pet. App. 13), "[t]he standards for judicial intervention are . . . narrowly drawn to assure the basic integrity of the arbitration process without meddling in it." A federal court must therefore determine not only whether an arbitrator has failed to disclose some association which, perhaps, should have been disclosed under the AAA rules, but also whether the undisclosed

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[12] Moreover, noting the "perfunctory investigation that Leatherby made into Clifford's background when the AAA first listed him as a possible arbitrator," the court of appeals stated: "If Leatherby had been worried about putting its fate into the hands of someone who might be linked in the distant past to the adversary's principal, it would have done more than it did to find out about Clifford. That it did so little suggests that its fear of a prejudiced panel is a tactical response to having lost the arbitration" (Pet. App. 17).

[13] The court noted (Pet. App. 11-12): "[T]he [Federal Arbitration Act] specifies limited grounds for setting aside an arbitration award. The only one relevant here is, 'Where there was evident partiality or corruption in the arbitrators, or either of them.' 9 U.S.C. § 10(b)."

association itself is one that reasonably suggests "evident partiality." Given the undisputed fact that Mr. Clifford and Mr. Stern had only a "distant and impersonal" association, as employees of the same company for a period of about two years ending more than 14 years before the arbitration began (Pet. App. 10), and had no contact whatever in the intervening period,[14] nondisclosure of that association, by itself, could not reasonably be deemed to constitute "evident partiality."

Finally, the court held that neither the AAA rules nor the Code of Ethics for Arbitrators require "disclosure of *every* former social or financial relationship with a party or a party's principals" (Pet. App. 7; emphasis added). The Code of Ethics not only explicitly provides that the duty of disclosure is "intended to be applied realistically" (Pet. App. 7), but also specifically relies on Justice White's statement in *Commonwealth Coatings Corp.* v. *Continental Casualty Co.*, 393 U.S. 145, 151-52 (1968), that "an arbitrator 'cannot be expected to provide the parties with his complete and unexpurgated business biography,' . . . [or] to disclose interests or relationships which are merely 'trivial' " (Pet. App. 7).

Leatherby filed a petition for rehearing and suggestion of rehearing en banc. After requiring the filing of a response by Merit, the court denied the petition (Pet. App. 43), with no judge in regular active service having requested a vote on the suggestion for rehearing en banc.

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[14] These facts not only were undisputed at the evidentiary hearing (*see* pages 6-7, *supra*), but apparently had been confirmed by Leatherby, which had interviewed other former co-employees of Mr. Stern and Mr. Clifford prior to the hearing (Tr. 444-46). Leatherby presumably would have called these persons as witnesses if their accounts had differed from those given by Mr. Stern and Mr. Clifford.

REASONS FOR DENYING THE WRIT

I.

THE COURT OF APPEALS CORRECTLY HELD THAT LEATHERBY DID NOT SATISFY THE THRESHOLD REQUIREMENTS FOR EXTRAORDINARY RELIEF UNDER FED.R.CIV.P. 60(b)

Leatherby asserts (Pet. 10-20) that this case warrants further review principally because the court of appeals allegedly misapplied this Court's holding in *Commonwealth Coatings Corp.* v. *Continental Casualty Co.*, 393 U.S. 145 (1968). Leatherby's assertion is insubstantial because, as we show below (*see* pages 16-24, *infra*), the holding of the court of appeals is consistent, not only with *Commonwealth Coatings* and the language and legislative history of the Federal Arbitration Act, but with every relevant reported decision. As a threshold matter, however, the court of appeals also correctly held (Pet. App. 15-17) that Leatherby had not carried its burden of establishing its entitlement to extraordinary relief under Fed.R.Civ.P. 60(b), and the correctness of the court's holding on this point logically precludes Leatherby from raising any of the other issues upon which it seeks review in this Court.

In asserting that it was entitled to relief from the judgment confirming the award, Leatherby rests on the district court's "finding" that Leatherby "had not learned of the relationship until April of 1982" (Pet. 22-23). However, the court of appeals correctly rejected this "finding" for the simple reason that the record does not support it (Pet. App. 16). Leatherby failed to offer any evidence that its officers and directors, as opposed to

its trial attorneys (who, by contrast, were paraded across the witness stand), did not know of Mr. Clifford's prior association with Mr. Stern. As the court of appeals correctly held (Pet. App. 16-17):

> Leatherby was required, and it failed, to support its Rule 60(b) motion with affidavits that its officers did not know of the relationship. It had to negate any inference that it had implicitly consented to have Clifford as an arbitrator knowing all it now knows but saying nothing.

Leatherby had the burden of producing such evidence because it was the moving party under Rule 60(b). As the court of appeals recognized, the purpose of Rule 60(b) is to undo substantial injustice, not to redress technicalities. *See DiVito* v. *Fidelity & Deposit Co.*, 361 F.2d 936, 939 (7th Cir. 1966) ("the relief provided by Rule 60(b) is equitable in character and to be administered upon equitable principles. . . . And, equity aids the vigilant"). If Leatherby's management actually knew of the prior association between Mr. Stern and Mr. Clifford, of course, Leatherby could not establish any "substantial danger of an unjust result" (Pet. App. 16). Since Leatherby failed to carry its burden on this critical point, its Rule 60(b) motion rested on a mere technicality.

The evidence Leatherby failed to produce also was peculiarly within its control, and Leatherby's failure to produce it therefore gives rise to the presumption that it would have been adverse.[15] Moreover, Leatherby affirma-

[15] "The rule is well established . . . that the failure to produce evidence, which under the circumstances would be expected, gives rise to a presumption against the party failing to produce it." *Neidhoefer* v. *Automobile Ins. Co.*, 182 F.2d 269, 271 (7th Cir. 1950). *Accord Fey* v. *Walston & Co.*, 493 F.2d 1036, 1053 (7th Cir. 1974); 2 E. Devitt and C. Blackmar, *Federal Jury Practice and Instructions*, §72.17 (3d ed. 1977).

tively thwarted Merit's attempt to inquire into the subject (*see* page 8, *supra*). A party's failure to produce its officers and directors to testify on a relevant issue on which they have critical knowledge is, as this Court has said, "itself persuasive that their testimony, if given, would have been unfavorable." *Interstate Circuit, Inc.* v. *United States,* 306 U.S. 208, 226 (1939). This is particularly true here, in view of Leatherby's admission that the insurance community is a relatively small group in which "they all know each other" (O.R. Item 123 at 3).[16]

Finally, Rule 60(b)(2) specifically requires that a motion based upon "newly discovered evidence" be supported by a showing that the evidence "by due diligence could not have been discovered in time to move for a new trial under Rule 59(b)." *See United States* v. *Walus,* 616 F.2d 283, 287-88 (7th Cir. 1980); *Flett* v. *W.A. Alexander & Co.,* 302 F.2d 321, 323-24 (7th Cir.), *cert. denied,* 371 U.S. 841 (1962).[17] Leatherby's motion was, of course, "[b]ased upon entries in Best's Insurance Reports for 1961-63" (Leatherby C.A. Br. 3), which were as readily available in 1977 as they were in 1982. Even assuming that this information would have been relevant to Mr. Clifford's suitability as

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[16] Leatherby's reliance on the testimony of its trial attorneys is also noteworthy because "[t]he production of weak evidence when strong is available can lead only to the conclusion that the strong would have been adverse." *Interstate Circuit, Inc.* v. *United States, supra,* 306 U.S. at 226.

[17] Although Leatherby styled its motion as one brought under Fed.R.Civ.P. 60(b)(6), the "catch-all" provision of the rule (Pet. App. 15), the motion was based only upon "newly discovered evidence" and was therefore plainly subject to the requirements of Rule 60(b)(2). *See, e.g., Corex Corp.* v. *United States,* 638 F.2d 119, 121 (9th Cir. 1981); *Bershad* v. *McDonough,* 469 F.2d 1333, 1336 n.3 (7th Cir. 1972). *See also DeFilippis* v. *United States,* 567 F.2d 341, 343 (7th Cir. 1977).

an arbitrator, and assuming further that the issue was one that properly could have been raised after the arbitration had commenced, Leatherby was not entitled to relief on this ground under Rule 60(b) because it failed to show that it could not have discovered the evidence with due diligence within the time allowed under Rule 59(b) for filing a motion for a new trial. Indeed, Leatherby failed to explain why, with due diligence, it could not have discovered the evidence prior to the time the judgment confirming the award had been entered, prior to the time its first Rule 60(b) motion had been denied, prior to the time its appeal had been taken, or, indeed, at any other time prior to April 1982, when Leatherby first raised the issue in its second Rule 60(b) motion. In fact, as the court of appeals noted (Pet. App. 17), the record shows that the only investigation ever made by Leatherby's attorneys was a perfunctory one made at the time Mr. Clifford was proposed as an arbitrator. *See* page 8, note 10, *supra*. Clearly, Leatherby failed to satisfy the due diligence requirement expressly imposed by Rule 60(b)(2).

Having lost not only before the arbitrators, but also in its attempt to block confirmation of the award and in its first Rule 60(b) motion, Leatherby cannot now invoke this technicality to further delay the consequences of the multimillion dollar fraud that it perpetrated more than 10 years ago. The court of appeals correctly held that Leatherby had not met the legal requirements for securing relief under Rule 60(b). That holding does not conflict with any decision of any other circuit, does not itself warrant review by this Court, and logically precludes consideration of any other issue upon which Leatherby seeks further review.

II.

THE HOLDING OF THE COURT OF APPEALS, THAT MR. CLIFFORD'S FAILURE TO DISCLOSE HIS STALE, LIMITED AND NONPECUNIARY ASSOCIATION WITH MR. STERN DID NOT CONSTITUTE "EVIDENT PARTIALITY" AS A MATTER OF LAW, IS NOT INCONSISTENT WITH ANY PRIOR HOLDING OF THIS OR ANY OTHER COURT

Not only did Leatherby fail to establish that its management was unaware of Mr. Clifford's prior association with Mr. Stern, but it was undisputed that: (a) the association was "distant and impersonal" during the period of their common employment and had terminated entirely 14 years before the commencement of the arbitration (Pet. App. 10); and (b) Mr. Clifford's nondisclosure to the AAA, whatever its motivation, clearly was not designed to aid Mr. Stern or Merit, because that nondisclosure antedated by two years Mr. Clifford's selection as an arbitrator in this case (Pet. App. 5). In substance, therefore, Leatherby's position is that an arbitrator's failure to disclose *any* prior association between a party and an arbitrator, no matter how impersonal, distant and stale, requires vacation of an award.

Leatherby's position seriously misconceives the proper function of the federal courts in determining whether to confirm an arbitration award. As the court of appeals correctly pointed out (Pet. App. 7), not even the AAA rules require disclosure of *every* prior association that an arbitrator may have had with one of the parties. The rules require disclosure of relationships that are "likely

to affect [the arbitrator's] impartiality" (AAA Rule 18).[18] Clearly, the limited association between Mr. Stern and Mr. Clifford, 14 years past, was not of that kind.

Even if the AAA rules did cover such a limited and stale association, however, the award would stand. The role of the federal courts under 9 U.S.C. §10(b) is not to enforce every technical requirement of the AAA rules, but to determine whether the award should be set aside on the statutory ground of "evident partiality." As the court of appeals stated (Pet. App. 13), "[t]he standards for judicial intervention are . . . narrowly drawn to assure the basic integrity of the arbitration process without meddling in it." The legislative history makes this point as graphically as it can be made: "The Courts are bound to accept and enforce the award of the arbitrators unless there is in it *a defect so inherently vicious* that, as a matter of common morality, it ought not be enforced." *Jt. Hearings before the Subcomm. on the Judiciary on S. 1005 and H.R. 646*, 68th Cong., 1st Sess. at 36 (1924) (emphasis added).

Leatherby's contention (Pet. 10-13) that the court of appeals misconstrued this Court's decision in *Commonwealth Coatings Corp.* v. *Continental Casualty Co.*, 393 U.S. 145 (1968), is incorrect for several reasons. First, Leatherby misstates the facts of that case. Contrary to Leatherby's assertion (Pet. 10), *Commonwealth Coatings*

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[18] Leatherby's statement of Rule 18 (Pet. 17) omits this critical part, which recites the general principle that the relationships to be disclosed are those "likely to affect [the arbitrator's] impartiality" (S.A. 3-4). The rule clearly contemplates some discretion in the arbitrator, and it surely was not unreasonable for Mr. Clifford to believe (*see* Tr. 98) that his prior association with Mr. Stern, whom he had not seen for 14 years, was not "likely to affect his impartiality."

did not involve an undisclosed "prior" relationship between an arbitrator and one of the parties. In fact, the arbitrator in that case had failed to disclose that one of the parties was a "regular" and "repeated" customer of the firm owned by the arbitrator, that the party had been paying substantial fees to the arbitrator's firm, and that "the relationship even went so far as to include the rendering of services [by the arbitrator's firm] on the very projects involved in the lawsuit" (393 U.S. at 146). As the court of appeals correctly noted (Pet. App. 13-14), the facts of *Commonwealth Coatings* are far different from those at bar, where the complained of association not only terminated 14 years before the arbitration began, but even then was nonpecuniary, distant and limited.

Second, Leatherby's statement of the holding (Pet. 10-11) in *Commonwealth Coatings* is wide of the mark. As the court of appeals correctly observed (Pet. App. 14), Justice Black's plurality opinion does not constitute the holding of that case, because the result depended upon the concurrence of Justices White and Marshall, who clearly were unwilling to join in the reasoning of that opinion. As Justice White stated (393 U.S. at 151-52), "it is enough for present purposes to hold, as the Court does, that where the arbitrator has . . . done more than trivial business with a party, that fact must be disclosed." In short, nothing in the holding of *Commonwealth Coatings* suggests that an award should be set aside, after three years of arbitration, merely because an arbitrator failed to disclose that he had known the president of one of the parties some 14 years before the arbitration began and had not seen him since.

As the court of appeals correctly held (Pet. App. 11-12), the question at issue in determining whether to vacate an

award is not whether, in hindsight, disclosure of a prior association might have been preferable, but whether the facts of a particular undisclosed association suffice to show "evident partiality." Thus, the myriad factual grounds upon which "evident partiality" may be asserted require that "cases of this type [be considered] on a case-by-case basis" (*U.S. Wrestling Federation* v. *Wrestling Division of AAU, Inc.*, 605 F.2d 313, 318 (7th Cir. 1979)). And, as Justice White stated in *Commonwealth Coatings* (393 U.S. at 151), an arbitrator cannot be expected to provide the parties with his unexpurgated business biography.[19] To set aside a unanimous award by three neutral arbitrators simply because one of them failed to disclose a 14-year-old, "distant and impersonal" nonpecuniary association would be to require that very kind of practically impossible disclosure and thus greatly undermine the finality of arbitration.[20]

The decision of the court of appeals is also consistent with the decisions of other federal courts, none of which has ever vacated an arbitration award for nondisclosure except where the undisclosed information concerned an ongoing pecuniary relationship between an arbitrator and

[19] The Code of Ethics for Arbitrators in Commercial Disputes makes the same point, stating: "arbitrators should disclose the existence of any interests or relationships which are *likely* to affect their impartiality or which *might reasonably* create the appearance that they are biased against one party or favorable to another" (Leatherby C.A. Br. App. 38; emphasis added).

[20] The court of appeals noted (Pet. App. 16): "[Leatherby's] counsel conceded at oral argument that his client would be bound to submit to a new arbitration proceeding if the award were set aside. But in the old proceeding Leatherby's own arbitrator voted against it. If we may believe that arbitrator's affidavit—and there is no reason not to—he did not regard this as a close case. According to the affidavit, both he and Merit's arbitrator pushed Merit's case harder than Clifford did." *See also* Pet. App. 12.

the prevailing party.[21] The Second Circuit, after exhaustively reviewing its own case law, has stated: "It is certainly fair to say that we have not been quick to set aside the results of an arbitration because of an arbitrator's alleged failure to disclose information." *Andros Compania Maritima, S.A.* v. *Marc Rich & Co., A.G.*, 579 F.2d 691, 700 (1978). Indeed, relationships far more suggestive of possible bias than the stale, limited, and nonpecuniary asso-

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[21] *See, e.g., Tamari* v. *Bache Halsey Stuart Inc.*, 619 F.2d 1196 (7th Cir.), *cert. denied*, 449 U.S. 873 (1980) (award upheld where witness had been hired by same company that employed arbitrator and person who appointed arbitrators was subsequently hired by one of the parties); *U.S. Wrestling Federation* v. *Wrestling Div. of AAU, Inc.*, 605 F.2d 313 (7th Cir. 1979) (award upheld where arbitrator belonged to law firm which had many relationships with university that was closely affiliated with prevailing party); *Andros Compania Maritima, S.A.* v. *Marc Rich & Co., A.G.*, 579 F.2d 691 (2d Cir. 1978) (award upheld where arbitrator and president of company involved in arbitration had close personal and professional relationship); *Transmarine Seaways Corp.* v. *Marc Rich & Co., A.G.*, 480 F.Supp. 352 (S.D.N.Y. 1979) (award upheld where arbitrator was president of company which was adversely aligned in another arbitration against the losing party); *Catz American Co.* v. *Pearl Grange Fruit Exchange, Inc.*, 292 F. Supp. 549 (S.D.N.Y. 1968) (award upheld where president of party was also member of board of arbitration association and personal friend of other arbitrators); *Ilios Shipping & Trading Corp., S.A.* v. *American Anthracite & Bituminous Coal Corp.*, 148 F.Supp. 698 (S.D.N.Y.), *aff'd*, 245 F.2d 873 (2d Cir. 1957) (award upheld where arbitrator was employee of insurance broker which did business with agent of party). *See also International Produce, Inc.* v. *A/S Rosshavet*, 638 F.2d 548 (2d Cir.), *cert. denied*, 451 U.S. 1017 (1981) (award upheld where arbitrator was called as non-party witness in unrelated arbitration between parties represented by the same law firms that were appearing in arbitration on which he served as arbitrator); *Sanko S.S. Co.* v. *Cook Indus., Inc.*, 495 F. 2d 1260 (2d Cir. 1973) (district court erred in denying evidentiary hearing on allegation that arbitrator had failed to disclose substantial and continuing business dealings between his employer and party to arbitration).

ciation between Mr. Clifford and Mr. Stern have been held insufficient to warrant vacation. *See International Produce, Inc.* v. *A/S Rosshavet*, 638 F.2d 548 (2d Cir.), *cert. denied*, 451 U.S. 1017 (1981); *Andros Compania Maritima, S.A.* v. *Marc Rich & Co., A.G., supra*, 579 F.2d 691.

As the court of appeals noted (Pet. App. 15), only the Eleventh Circuit has ever vacated an arbitration award on grounds remotely similar to those advanced here, and that case is distinguishable on fundamental grounds. In *Middlesex Mutual Ins. Co.* v. *Levine*, 675 F.2d 1197 (11th Cir. 1981), an award was vacated because one of the arbitrators had failed to disclose his pecuniary interest in ongoing litigation involving one of the parties to the arbitration (*id.* at 1199-1202). The ongoing pecuniary relationship at issue in *Middlesex* is readily distinguishable from the limited and nonpecuniary association between Mr. Stern and Mr. Clifford, which spanned only about two years in the early 1960's, and consisted of "little professional contact" during that period and "no social contacts then or since" (Pet. App. 3).

Nor is the decision below inconsistent with the three state court decisions upon which Leatherby relies (Pet. 11-12). In each of those cases, the arbitration award was vacated because the arbitrator had failed to disclose the existence of an *ongoing* commercial relationship with one of the parties. *See Barcon Associates, Inc.* v. *Tri-County Asphalt Corp.*, 430 A.2d 214, 216-17 (N.J. 1981); *Richco Structures* v. *Parkside Village, Inc.*, 263 N.W.2d 204, 208 (Wis. 1978); *J.P. Stevens & Co.* v. *Rytex Corp.*, 312 N.E.2d 466, 467-68 (N.Y. 1974).[22]

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[22] Moreover, in each of those cases the courts were construing state statutes governing arbitration awards, not 9 U.S.C. §10(b). *See Barcon Associates, Inc.* v. *Tri-County Asphalt Corp., supra*, 430 A.2d at 215; *Richco Structures* v. *Parkside Village, Inc., supra*, 263 N.W.2d at 210; *J.P. Stevens & Co.* v. *Rytex Corp., supra*, 312 N.E.2d at 467.

(footnote continued)

Leatherby also contends (Pet. 16-18) that the decision below warrants review because the court of appeals allegedly ignored the fact that Leatherby did not get what it bargained for—an arbitration in strict compliance with the AAA rules. This contention does not warrant review for several reasons:

First, Leatherby premised its entitlement to relief in the courts below on the statutory ground of "evident partiality" and raised this contractual issue for the first time in its petition for rehearing in the court of appeals (C.A. Pet. R. 10). It would therefore be improvident for this Court to grant review to decide this question on the present record, even if the issue were an appropriate subject for review by this Court, which it is not.

Second, Leatherby's contention is without merit in any event because, in contracting for arbitration under the AAA Rules, Leatherby was guaranteed only that the arbitrators would disclose those relationships which, in their view, might reasonably affect their impartiality.[23]

Finally, Leatherby's position is at odds with the basic policy of the Federal Arbitration Act, which per-

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(footnote continued)

A fourth case, upon which Leatherby relied heavily below (C.A. Pet.R. 5-6), *Northwest Mechanical, Inc.* v. *Public Utilities Comm'n*, 283 N.W.2d 522, 523 (Minn. 1979), involved a "substantial" commercial relationship which, although not ongoing in the sense of being uninterrupted, was both recent and reasonably subject to revival. The relationship in *Northwest Mechanical*, which was similar to that involved in *Commonwealth Coatings*, is clearly unlike that involved here.

[23] Indeed, Leatherby now seeks considerably more than it bargained for because AAA Rule 27 provides that an award ordinarily may be made by a simple majority vote of the arbitrators (S.A. 4, 11). Moreover, Leatherby expressly agreed that it would abide by a unanimous decision rendered by two arbitrators if the third should be unable to act, at least in the event of sickness or accident (S.A. 15).

mits the vacation of an award only on one of the stated statutory grounds, which are to be strictly construed if the benefits of arbitration, as a speedy and inexpensive alternative to litigation, are to be realized. *E.g., Diapulse Corp.* v. *Carba, Ltd.*, 626 F.2d 1108, 1110 (2d Cir. 1980). *See generally Wilko* v. *Swan,* 346 U.S. 427, 431-32 (1953). In effect, Leatherby seeks to expand the scope of judicial review far beyond that provided by the statute, which, as invoked here, requires a finding of "evident partiality." Leatherby, in choosing arbitration to resolve this dispute, bargained for this statutory standard of review, which the court of appeals correctly applied.[24]

In sum, the decision below is consistent with this Court's holding in *Commonwealth Coatings* and with every relevant reported decision.

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[24] The cases upon which Leatherby relies (Pet. 17-18) are inapposite. In *Tamari* v. *Conrad,* 552 F.2d 778 (7th Cir. 1977), the court affirmed the dismissal, on immunity grounds, of a civil action against the arbitrators. In a dictum (*id.* at 781), the court simply noted that its decision should not be construed to have any bearing on the plaintiffs' claim that the selection and composition of the panel violated the terms of the agreement to arbitrate, which the plaintiffs had raised in a separate litigation. In *Food Handlers Local 425* v. *Pluss Poultry, Inc.*, 260 F.2d 835 (8th Cir. 1958), one of the parties to a labor dispute refused to arbitrate. The opposing party picked an arbitrator and obtained a favorable decision, despite the fact that the arbitration agreement required a tri-partite arbitration panel selected by both parties. In declining to give effect to the single arbitrator's award, the court stated, as an alternative holding, that such fundamental noncompliance with the arbitration agreement was fatal (*id.* at 837). Similarly, in *Local 227, Int'l Hod Carriers* v. *Sullivan*, 221 F.Supp. 696, 700 (E.D.Ill. 1963), "[t]here was not the remotest attempt to follow [the arbitration clause of] the collective bargaining agreement." Finally, in *Carr* v. *American Ins. Co.*, 152 F.Supp. 700 (E.D.Tenn. 1957), an award was invalidated under the Tennessee arbitration statute because the arbitrators had totally ignored their specific instruction to ascertain cash values and losses for individual items covered by fire insurance policies.

III.

THE DECISION BELOW WILL ENHANCE, RATHER THAN IMPEDE, ARBITRATION

Leatherby has also attempted to support its argument on alleged considerations of public policy, asserting that the decision below will discourage resort to arbitration by forcing "every party to become a detective before arbitration begins" (Pet. 20). As the facts of this case show, however, it is Leatherby's theory that would discourage arbitration.

First, Leatherby produced no evidence—not even an affidavit—to show that its officers and directors, as opposed to its trial attorneys, ever were unaware of Mr. Clifford's past association with Mr. Stern (Pet. App. 16). Second, Leatherby's attorneys, at best, did virtually nothing to investigate the backgrounds of the arbitrators until long after Leatherby had lost the arbitration, its several attempts to block confirmation of the award, and its first Rule 60(b) motion (*see* Pet. App. 17). Finally, the undisputed evidence shows that Mr. Stern and Mr. Clifford not only had little contact during the two years that they were employed by the same company, but had not even seen each other in the 14 years that followed (Pet. App. 4, 10).

If these facts were deemed sufficient to set aside an arbitration award on the statutory ground of "evident partiality," no reasonable person would ever submit to arbitration. The benefits normally attributed to arbitration, as a speedy and inexpensive alternative to litigation, would indeed be illusory if the losing party could abrogate a fairly conducted arbitration merely by raising some remote association between an arbitrator and the prevailing party long after the arbitration had been completed. Leatherby's persistent and purely technical attack on the

arbitration award in this case is merely a testimonial to "the ingenuity of attorneys for the losing party to find a plausible basis for challenge" (*U.S. Wrestling Federation v. Wrestling Division of AAU, Inc.*, 605 F.2d 313, 318 (7th Cir. 1979)), which the court of appeals correctly rejected.

IV.

THE COURT OF APPEALS GAVE PROPER DEFERENCE TO THE DISTRICT COURT'S FINDINGS OF FACT

Leatherby contends (Pet. 23-25) that the court of appeals erred in rejecting the district court's "findings of fact" without deciding that those findings were clearly erroneous, as required by Fed.R.Civ.P. 52(a). As we have noted (*see* pages 8-9, *supra*), the court of appeals did indeed reject two findings made by the district court—for the simple reason that there was *no* record evidence to support them. That was far from improper.

Apart from these two instances, however, Leatherby's argument is concerned not with the district court's "findings of fact," which the court of appeals never questioned, but with the district court's ultimate conclusions of law, to which the clearly erroneous standard does not apply. For instance, Leatherby is simply wrong in asserting (Pet. 24) that the court of appeals rejected the district court's finding as to Mr. Clifford's credibility.

It is true that the district court commented adversely on Mr. Clifford's credibility (Pet. App. 20), but it did so in connection with the explanation he gave for having

failed to disclose his prior employment with CIC. Although the district court found Mr. Clifford's explanation unsatisfactory, his reasons for not disclosing his prior employment could not have had anything to do with an intention to favor Mr. Stern or Merit, since Mr. Clifford had failed to disclose his CIC employment to the AAA more than two years before he was considered for this arbitration. *See* page 9, note 11, *supra*. The court of appeals did not question the district court's finding as to Mr. Clifford's credibility because, as the court explained (Pet. App. 4), the facts material to Mr. Clifford's tenure at CIC and to the nature of his association with Mr. Stern were independently corroborated both by Mr. Stern and Mr. Rotheiser, whose credibility was not at issue. Moreover, their testimony was not disputed at the hearing, even though Leatherby had interviewed other former CIC employees, who presumably would have been called to testify if they could have contradicted it. *See* page 11, note 14.

The court of appeals did, however, reject the district court's conclusion that nondisclosure of the stale, limited, and nonpecuniary association evidenced by the undisputed record facts was sufficient, as a matter of law, to require vacation of the award under the statutory standard of "evident partiality." This conclusion was not a finding of fact but an ultimate conclusion of law, or, at most, a conclusion derived from "a mistaken impression of applicable legal principles," to which the clearly erroneous standard does not apply. *Inwood Laboratories, Inc.* v. *Ives Laboratories, Inc.*, 456 U.S. 844, 855 n.15 (1982); *see United States* v. *Singer Mfg. Co.*, 374 U.S. 174, 194 n.9 (1963); *United States* v. *United States Gypsum Co.*, 333 U.S. 364, 394 (1948).

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted,

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DATED: November 15, 1983

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APPENDIX

APPENDIX

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

In the Matter of the Arbitration between

MERIT INSURANCE COMPANY, Petitioner, Counter-respondent	)	
and	)	No. 80 C 6758
LEATHERBY INSURANCE COMPANY, a/k/a WESTERN EMPLOYERS INSURANCE COMPANY, Respondent, Counter-petitioner.	)	

MEMORANDUM OPINION

CHARLES P. KOCORAS, District Judge:

This matter comes before the court on the petition of Merit Insurance Company ("Merit") to confirm an arbitration award which was rendered in Chicago on December 1, 1980 in the amount of $10,675,000. The respondent Leatherby Insurance Company ("LIC") moves to vacate, to modify, or to correct that award.

This court cannot and need not recite the entire history of the arbitration proceeding. Three arbitrators of the American Arbitration Association, who have professional backgrounds in law and who are familiar with the insurance industry, took part in the proceedings in Chicago, Illinois. The arbitration endured for three years, proceeded for over 120 sessions, and produced a transcript in excess of 16,000 pages. The arbitrators considered

either the live or deposition testimony of more than twenty five witnesses; thousands of pages of documents, including corporate records and correspondence, were presented at the hearings. The petitioner estimates that the arbitrators spent more than 1100 hours in independent study during the three year proceeding. For purposes of their motions before this court, the parties have filed more than 180 pages of briefs with over thirty exhibits.

Merit and LIC executed a Reinsurance and Assumption Agreement on October 20, 1972 in New Jersey. In the agreement, Merit reinsured all claims that the insured could make against insurance policies issued by LIC through its "retrospective" agent, General Auto Placement Inc. ("GAP"). The "retrospective agency" between the insurer LIC and the agent GAP determines the agent's commissions by retrospectively computing the profitability of the insurance; in this arrangement, the agent issues his own policies and establishes his own department for the investigation and settlement of claims against the policyholders. After the parties entered into the agreement in October of 1972, Merit effectively stepped into the position of LIC with respect to the insurance policies that had been issued on LIC's behalf by GAP.

The gist of Merit's complaint was that LIC failed to disclose several material facts with respect to the reinsurance transaction and that Merit would not have executed the agreement to reinsure the policies procured by GAP had LIC disclosed the facts. In particular, GAP had continually violated the terms of its retrospective arrangement with LIC by engaging in fraudulent practices such as diverting premiums and closing its claim files prematurely in order to present a false image of its profitability. More important, GAP had failed to make adequate incre-

ments to its reserve funds for outstanding insurance claims and it had denied LIC access to its books or records.

According to Merit, LIC's president discovered that GAP's business was deteriorating and that GAP had deceived LIC in 1971. In August of that year, LIC's president advised GAP's president, Leonard Lebowitz, to find another insurance carrier that would reinsure the policies at issue. (Merit Brief in Supp. of Pet. to Confirm, pp. 16-17). LIC's president testified that he did not cancel GAP's retrospective arrangement at that time because of his hope that GAP would obtain another carrier to reinsure the GAP business for which LIC was ultimately liable. (Merit Brief, p. 17).

Jerome Stern, president of Merit, was solicited by GAP in April, 1972 to become a new insurance underwriter for GAP's operation. The statements of independent auditors indicated that GAP's business was operated properly and that its loss ratio was favorable. Having reviewed those statements, Mr. Stern met with Mr. Lebowitz in April, 1972. After the meeting, Mr. Stern obtained a favorable report from Dun & Bradstreet on GAP as well as a credit and reinsurance reference. In view of those promising indications, Merit agreed to make GAP its retrospective agent for any business procured by GAP after July, 1972. Further, Mr. Lebowitz of GAP ultimately persuaded Merit to reinsure those policies that had been written by GAP on behalf of LIC prior to July, 1972. As a result, LIC and Merit executed the Reinsurance and Assumption Agreement on October 20, 1972 which underlies the parties' dispute.

GAP's business had continued to deteriorate from August, 1971 to February, 1972. In particular, GAP improperly reduced its claim reserves and arbitrarily closed

some of its claim files in order to create a fictitious impression of its outstanding liabilities. LIC's vice president determined that GAP had defrauded LIC, and the deteriorating relationship between LIC and GAP culminated in a lawsuit in a New Jersey state court. LIC obtained a judgment in June, 1972 for $1,489,000 against GAP, and several court orders provided LIC with direct access to GAP's claim files. During the period from June, 1972 to October 20, 1972, LIC pursued its suit against GAP. Despite the ongoing litigation between the parties, LIC's attorney allegedly advised LIC to suspend any action in court against GAP that could place the pending negotiations between GAP and Merit in jeopardy. In addition, Merit alleges that LIC concealed the adverse facts concerning its relationship with GAP that could affect Merit's decision to complete the reinsurance transaction with GAP.

From 1969 to 1972, GAP failed to maintain a proper level of reserves for individual claim files. Because GAP failed to keep adequate reserves, LIC placed additional funds in a separate account, known as an IBNR account, in order to cover the outstanding claims arising from GAP's business. According to Merit, the total reserves actually held by GAP and LIC did not comport with the amount listed in their usual reserve funds. (Merit Brief, p. 18). Specifically, LIC had concealed from Merit the placement of over $1,000,000 in actual cash reserves into the IBNR account. (Merit Brief, p. 21). As a result, Merit executed the reinsurance agreement without knowledge of the $1,200,000 IBNR reserve fund or of other facts concerning LIC's adverse relationship with GAP.

LIC obtained a clear benefit by depositing over $1,000,000 into its "secret" IBNR reserve account. As previously stated, LIC had obtained a judgment against GAP in the amount of $1,489,000 in a New Jersey state

court. Because Merit acquired the GAP policies without receipt of the total reserves from the carrier, LIC could apply the $1,000,000 in the IBNR account to the judgment which it had obtained against GAP. In that way, GAP would only need to pay $489,000 to LIC in order to satisfy its obligation. According to Merit, LIC knew that the insurance claims which it transferred to Merit would require more reserves than it had concealed in the IBNR account. If GAP's deteriorating business had not been reinsured by Merit, LIC would have had to bear the losses incurred on the claims. According to the testimony of LIC's comptroller, Merit suffered a minimum loss of $1,000,000 as soon as the Reinsurance and Assumption Agreement was executed. (Merit Brief, p. 22).

Arbitration began in 1977 by order of this court on June 20, 1977 in the case of *Merit Insurance Company* v. *Anthony Colao*, 75 C 899. Judge Julius Hoffman issued his order in response to LIC's motion for arbitration of Counts VI, VII and VIII of Merit's Third Amended Complaint. Those Counts alleged that the defendants defrauded Merit in the purchase of the insurer's rights and obligations under the policies written by the agent GAP in New Jersey. Merit sought actual damages of $6,000,000 and exemplary damages of $9,000,000.

LIC had filed a "demand for arbitration" on December 27, 1976, more than six months before Judge Hoffman issued his order, to the American Arbitration Association. In that demand, LIC stated that "Merit Insurance Company claims in excess of $2,000,000 damages." (Exh. A, Merit Brief). Subsequent to Judge Hoffman's order, LIC filed a second "demand for arbitration" on June 27, 1977 in which it stated that "Merit Insurance Company claims in excess of $6,000,000 damages." (Exh. B, Merit Brief). In its trial brief before the arbitrators, Merit Insurance

Company sought a total of $21,684,607 in compensatory damages, including lost profits, and a total of $7,228,202 in punitive damages. (Merit Trial Brief, p. 175).

In addition, Merit Insurance Company submitted several "tables on damages" as exhibits in the arbitration. Merit Exhibit 41 in Arbitration, which is dated July 12, 1978, shows total compensatory damages, including foregone business, in the amount of $10,529,186. (Exh. 14, LIC Brief). Merit Exhibit 115 in Arbitration, which is dated June 16, 1980, shows total damages for the same categories in the amount of $13,669,687. (Exh. 15, LIC Brief).

The Reinsurance and Assumption Agreement of October 20, 1972 contains an arbitration clause stating that any controversy arising out of or relating to the contract shall be settled by arbitration in accordance with the Rules of the American Arbitration Association in "Camden County, New Jersey", and that judgment upon the award "may be entered in any New Jersey Court having jurisdiction thereof." (LIC Brief, Exh. 1, para. 17). Another clause states that "this agreement shall be construed and interpreted under the laws of the State of New Jersey." (LIC Brief, Exh. 1, para. 18). Because LIC requested the arbitration to proceed in Chicago, Illinois, there is no dispute for purposes of the parties' motions that Chicago was the proper site of the proceedings. Further, the parties agree that the arbitrators in Chicago were required to apply the law of New Jersey to the disputed issues. Finally, both this court and the federal district court in New Jersey ruled that the district court for the Northern District of Illinois is the appropriate forum for review of the Chicago arbitration proceedings.

After the arbitrators rendered their award in Merit's favor on December 1, 1980, Merit's counsel sent a letter on December 2, 1980 to the arbitrators which was designated as a "motion to clarify award." (LIC Brief, Exh. 3). The

arbitrators had unanimously awarded "Merit Insurance Company the total sum of $10,675,000 for all damages claimed by Merit Insurance Company in this arbitration proceeding." (LIC Brief, Exh. 2). In its motion to clarify, Merit assumed that the foregoing phrase was not intended to include punitive damages, and it asked the arbitrators to specify that the words "all damages" should be construed as "all compensatory damages." (LIC Brief, Exh. 3). The arbitrators issued the requested clarification on December 11, 1980, which stated in part that the sum was awarded to Merit "as compensatory damages only and does not include any sum for punitive damages"; they also wrote that "there is no intent by the Arbitrators to award any punitive damages in this proceeding." (LIC Brief, Exh. 7).

Respondent LIC asks this court to vacate or to modify the arbitration award for several reasons. LIC's principal argument is that the award of $10,675,000, when compared with Merit's actual out-of-pocket damages of between one and three million dollars, reflects the arbitrators' failure to follow the applicable law of New Jersey. Similarly, respondent contends that the award lacks "fundamental rationality", violates public policy, and includes punitive damages in violation of both New Jersey and federal law. Furthermore, respondent argues that "newly discovered evidence" suggests fraud in Merit's procurement of the award; that the arbitrators failed to allow a 50% set-off under the applicable contribution statute of New Jersey; and that the record demonstrates bias and prejudice on the part of the arbitrators. In support of those and other contentions, respondent cites the relevant subparagraphs of the Federal Arbitration Act, 9 U.S.C. §10(a)-(d).

This district court has original jurisdiction of motions to vacate and motions to confirm awards pursuant to the

Federal Arbitration Act, 9 U.S.C. §§9 and 10, where interstate commerce is involved. *See, eg., Shearson Hayden Stone, Inc.* v. *Liang*, 493 F. Supp. 104, 106 (N.D. Ill. 1980), *aff'd* 653 F.2d 310 (7th Cir. 1981). The Reinsurance and Assumption Agreement between Merit Insurance Company and Leatherby Insurance Company is a contract that affects interstate commerce. Moreover, the agreement's provision which states that the law of New Jersey must govern the arbitration does not bar review of the award in a federal district court. *See, eg., Hetherington & Berner, Inc.* v. *Melvin Pine & Co.*, 256 F.2d 103 (2d Cir. 1958). For purposes of this court's review of the arbitration award, the Federal Arbitration Act rather than state arbitration law applies.

This court's power to set aside the arbitration award is limited to the grounds set forth in 9 U.S.C. §10. *Shearson Hayden Stone, Inc.* v. *Liang, supra*, 653 F.2d at 313; *Tamari* v. *Bache Halsey Stuart Inc.*, 619 F.2d 1196, 1198 n.2 (7th Cir. 1980).[1] The respondent LIC appears to rely

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[1] 9 U.S.C. §10 provides:

In either of the following cases the United States Court in and for the district wherein the award was made may make an order vacating the award upon the application of any party to the arbitration—

(a) Where the award was procured by corruption, fraud or undue means.

(b) Where there was evident partiality or corruption in the arbitrators, or either of them.

(c) Where the arbitrators were guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the controversy; or of any misbehavior by which the rights of any party may have been prejudiced.

(d) Where the arbitrators exceeded their powers, or so imperfectly executed them that a mutual, final and definite award upon the subject matter submitted was not made.

on §§10(a), (b), (c) and (d) in support of its motion to vacate the award.

I.

The respondent LIC contends that the award should be vacated because the arbitrators failed to follow the applicable law of New Jersey in making their decision. The parties do not suggest, however, that their dispute was improperly assigned to arbitration under the terms of the arbitration clause in their written agreement.

It is well settled that an arbitration award will not be vacated on the ground that the arbitrators misinterpreted applicable law. *Nat. R.R. Pass. Corp.* v. *Chesapeake & O. Ry.*, 551 F.2d 136, 143 (7th Cir. 1977); *Sobel* v. *Hertz, Warner & Co.*, 469 F.2d 1211, 1214 (2nd Cir. 1972). As Judge Sprecher noted, some courts have construed the Supreme Court's decision in *Wilko* v. *Swan*, 346 U.S. 427, 74 S. Ct. 182, 98 L. Ed. 168 (1953), to permit vacation of an arbitration award which displays a "manifest disregard" of applicable law. *Nat. R.R. Pass. Corp.* v. *Chesapeake & O. Ry., supra*, 551 F.2d at 143. Even those courts which have adopted that view, however, have concluded that its application is "severely limited." *Id.* at 143.

This court's review of the arbitration award is somewhat troublesome in the instant case because the arbitrators gave no reasons for their award or decision. It is clear, however, that they are not required to do so. *See, eg., Shearson Hayden Stone, Inc.* v. *Liang, supra*, 653 F.2d at 312. As Judge Feinberg observed, "the extent of an arbitrator's obligation to explain his award is necessarily related to the scope of judicial review", and that review becomes especially difficult insofar as it attempts to define "manifest disregard" of applicable law. *Sobel* v. *Hertz, Warner & Co., supra*, 469 F.2d at 1214. The Seventh

Circuit Court of Appeals has shared the Second Circuit's reservations about whether the *Wilko* decision actually intended to add "manifest disregard" of the law to the statutory grounds for vacating an award in 9 U.S.C. §10. *See Nat. R.R. Pass. Corp.* v. *Chesapeake & O. Ry., supra,* 551 F.2d at 143 n.9. As a practical matter, the courts can encounter great difficulty in distinguishing between an arbitrator's "erroneous interpretation" of applicable law and his "manifest disregard" of it. *Id.* at 143 n.9. Moreover, "since arbitrators have no obligation to state the rationale underlying their award, there may be no basis whatsoever for a court to determine whether they have manifestly disregarded the law or simply misinterpreted it." *Id.* at 143 n.9.

The parties submitted detailed legal briefs on various issues under New Jersey law to the arbitrators. Counsel also presented a variety of expert witnesses as well as extensive oral summation in the course of the three-year proceeding; parties specifically addressed themselves to conflicting theories for the computation of damages which Merit had sustained. In addition, the parties' briefs in arbitration included arguments on whether lost profits or consequential damages may be properly recovered in an action for fraud under New Jersey law. The arbitrators "had the benefit of extremely detailed submission to arbitration", thorough memoranda of law, and oral summations of counsel which indicate a number of theories upon which the arbitrators may have decided. *See also Sobel* v. *Hertz, Warner, supra,* 469 F.2d at 1215. This court will not and need not impose its view on the validity of the theories underlying possible grounds for the award; it is sufficient if the award can in "any rational way" be derived from the applicable law of New Jersey. *See, eg., Ludwig Honold Mfg. Co.* v. *Fletcher,* 405 F.2d 1123, 1128 (3rd Cir. 1969).

As the petitioner's briefs both before the arbitrators and this court have correctly stated, there is ample support in New Jersey law for the inclusion of lost profits in damages incurred because of fraud. The courts of New Jersey have consistently held that "loss of profits, where based on sound fact and not on mere opinion evidence, is recognized as a proper measure of damages if capable of being estimated with a reasonable degree of certainty." *Henry Clay* v. *Jersey City*, 74 N.J. Super. 490, , 181 A.2d 545, 549 (1962) [cites omitted]. Further, the Supreme Court of New Jersey has recognized that "the victims of fraud are entitled to compensation for every wrong which was the natural and proximate result of the fraud." *Zeliff* v. *Sabatino*, 15 N.J. 70, , 104 A.2d 54, 56 (1954). Those and other cases were cited in the arbitration briefs and it is therefore clear that the arbitrators did not simply ignore the applicable law. The arbitrators' possible reliance upon such cases or theories does not provide a basis for vacating the award.

Respondent's argument that the arbitrators awarded an excessive amount of damages in violation of New Jersey law boils down to an assertion that they reached the wrong result from conflicting evidence and testimony. This court may not vacate the award on that ground. *See, eg., Shearson Hayden Stone* v. *Liang*, *supra*, 653 F.2d at 312. The arbitrators were free to compute the amount of damages from the conflicting evidence before them. Similarly, this court cannot reconsider the evidence in order to determine whether any independent investigation that Merit may have undertaken was sufficient to negate its reliance on LIC's false representations. It is clear that the arbitrators, having considered the evidence, concluded that Merit was entitled to rely upon LIC's representations.

Respondent also contends that the award of $10,675,000 should be vacated under 9 U.S.C. §10(d) because it lacks fundamental rationality. Specifically, respondent asserts that the amount of the award is irrational in view of respondent's failure to report $1,000,000 in claim reserves in the reinsurance transaction. The Seventh Circuit has not decided whether an arbitration award may be vacated under the Federal Arbitration Act on the ground of "irrationality." *Shearson Hayden Stone* v. *Liang, supra,* 653 F.2d at 312; *Nat. R.R. Pass. Corp.* v. *Chesapeake & O. Ry., supra,* 551 F.2d at 142 n.5. A court also faces great difficulties in attempting to assess the rationality of an award where the arbitrators have given no reasons for the award.

Judge Flaum used the same analysis in determining whether an arbitration award was either "fundamentally irrational" or in "manifest disregard" of the law under 9 U.S.C. §10(d). *Shearson Hayden Stone* v. *Liang, supra,* 493 F. Supp. at 108. In the instant case, there was ample evidence submitted to the arbitrators, both in the form of briefs and expert testimony, that could support the amount of the award. Indeed, a review of that evidence and the applicable law compels the conclusion that the arbitrators were following the law in their award and did not manifestly disregard it or mandate a fundamentally irrational result. There is no basis to conclude that section 10(d) of the Act was violated.

II.

Respondent LIC argues that the large amount of the arbitration award indicates that it is inherently punitive because it vastly exceeded Merit's out-of-pocket losses. In addition, respondent contends that the arbitrators' clarification of their award was ineffective.

In response to Merit's motion, the arbitrators issued a clarification of their award on December 11, 1980 which stated that the sum of $10,675,000 was awarded to Merit "as compensatory damages only and does not include any sum for punitive damages." (LIC Brief, Exh. 7). Further, the clarification stated that "there is no intent by the Arbitrators to award any punitive damages in this proceeding." (Exh. 7). In the course of the arbitration proceedings, Merit submitted various exhibits and expert testimony that could support an award in excess of $10,675,000 f · compensatory damages, including lost profits. (See, eg., Merit Trial Brief, p. 175; Exh. 15, LIC Brief; Plotkin testimony, etc.).

Arbitrators may use their discretion in the computation of damages, and a court may not lightly disturb the arbitrators' exercise of that discretion where the evidence and theories presented in arbitration could have sustained the sum of the award. Judicial review of the arbitrators' method of computation is especially restricted where no reasons have been given for the award. The respondent's repeated assertion that "punitive damages" were awarded will not suffice to vacate an arbitration award where discretion is used in the computation of damages; only where the damages are genuinely intended to be punitive should the courts vacate the award. *See, eg., John T. Brady & Co.* v. *Form-Eze Systems, Inc.*, 623 F.2d 261 (2nd Cir. 1980), *cert. denied* 101 S. Ct. 786 (1980) citing *Board of Education* v. *Niagara-Wheatfield Teachers Ass'n*, 46 N.Y.2d 553, 558, 389 N.E.2d 104, 10[illegible] (1979).

In this case, the arbitrators did not label the award of $10,675,000 as "punitive" and there is nothing to indicate a genuine intention that the award punish the respondent. *Id.* at 264. On the contrary, the clarification of the award made it absolutely clear that the arbitrators did not in-

tend to include punitive damages in any part of the award. Courts have generally accorded the narrowest of readings to the Act's authorization to vacate awards where the arbitrators have exceeded their powers under 9 U.S.C. §10(d). *Id.* at 264. In this case the arbitrators did not characterize the award as punitive and there is no reason for this court to assume that it was. Moreover, respondent has failed to convince this court that the arbitrators' clarification was either invalid or improper.

Respondent LIC also contends that the arbitration award should be vacated because it violates public policy. Although contravention of public policy is not one of the specific grounds for vacation set forth in section 10 of the Federal Arbitration Act, an award may be set aside if it compels the violation of law or is contrary to a well accepted and deep rooted public policy. *Diapulse Corp. of America* v. *Carba, Ltd.*, 626 F.2d 1108, 1110 (2nd Cir. 1980). In support of its argument, respondent asserts that the arbitrators failed to decide the dispute in accordance with New Jersey law and that the award was both punitive and speculative.

There is certainly nothing in the award that compels the violation of law. The arbitrators may have determined that lost profits may be properly recovered for fraud under New Jersey law, and they explicitly stated that punitive damages constituted no part of the awarded sum. As a result, the award did not infringe any deep rooted public policy against punitive damages. Moreover, compensatory damages do not become punitive whenever they are somewhat speculative. *See, eg., John T. Brady & Co.* v. *Form-Eze Systems, Inc., supra*, 623 F.2d at 264. There is no public policy prohibiting an arbitration tribunal from awarding a defrauded party com-

pensatory damages, including lost profits, that are the proximate result of the fraudulent transaction.

III.

Respondent argues that the award should be vacated for fraud under §10(a) of the Act because Merit's annual financial statement, which was released on March 1, 1981, indicates that the arbitrators relied upon erroneous estimates for Merit's reserves. The reserve estimates for 1977, 1978, and for the first half of 1979 suggested that Merit's insurance business was extremely profitable, whereas the subsequent statement of March, 1981 suggests that Merit was substantially underreserved. LIC attempts to rely on the "newly discovered evidence" that became available on March 1, 1981 to vacate the award made on December 1, 1980.

The Federal Arbitration Act does not allow vacation of an award for new evidence. *Shearson Hayden Stone, Inc.* v. *Liang, supra,* 653 F.2d at 313. Moreover, no case expressly holds that new evidence or nondisclosure of evidence constitutes "fraud" under section 10(a). *Id.* at 313. This court has also recognized that newly discovered evidence, even if it could not have been discovered prior to the arbitration proceeding, may not be used to directly contradict the evidence presented during the arbitration proceeding. *Shearson Hayden Stone, Inc.* v. *Liang, supra,* 493 F. Supp. at 109 citing *Washington-Baltimore Newspaper Guild Local 35* v. *Washington Post Co.,* 442 F.2d 1234, 1238-39 (D.C. Cir. 1971).

As Merit has stated in its brief, all of its financial reports that existed as of December 1, 1980 were made available to the arbitrators. The arbitrators had the discretion to use and to assess the available reports as they

saw fit. The gist of respondent's argument is that the arbitration should be reopened whenever new financial reports are issued on Merit Insurance Company in order to enable more accurate projections of the company's profitability. If respondent were correct, the arbitration in this case would never end. The arbitrators were free to consider all of the financial data that Merit had at its disposal during the course of the proceedings; they could do no more. In effect, respondent's argument implies that any arbitration award, which is based in part on reasonable estimates of lost profits, should be vacated whenever the subsequent financial statements of the aggrieved party do not comport with those estimates. Such a result would wreak havoc upon the arbitration process, and this court will not vacate the award on those grounds.

IV.

Respondent also argues that the arbitrators ignored the applicable law of New Jersey because they refused to allow a pro rata setoff of fifty percent on the award. A New Jersey statute, N.J.S.A. Ch. 2A-53A-1 *et seq.*, provides for a right of contribution among joint tortfeasors. Because Merit had settled its claim with GAP's president, Leonard Lebowitz, respondent LIC contends that its own liability as the remaining tortfeasor should be reduced by half. Respondent claims that the arbitrators imperfectly executed their powers under §10(d) by failing to apply the setoff under the New Jersey contribution statute. Respondent concedes that it asserted its right to the setoff in the arbitration proceedings by extensive briefs and argument. (LIC Brief, p. 49).

Respondent's claim here reduces to the proposition that the arbitrators either ignored or misapplied New Jersey's contribution statute. There is no basis upon which this

court may conclude that the arbitrators "manifestly disregarded" the applicable law. First, the arbitrators may have concluded upon consideration of the parties' briefs and evidence that Mr. Lebowitz was an "agent" of LIC. If that were so, LIC and Lebowitz as principal and agent could not be treated as joint tortfeasors under the New Jersey statute. Second, even if the arbitrators regarded Lebowitz as a joint tortfeasor, there is nothing to indicate that the arbitrators failed to apply the contribution statute. Respondent assumes that Lebowitz was equally liable for the transaction, and that LIC is therefore entitled to a fifty percent setoff. The arbitrators, however, may have concluded that Lebowitz was responsible only to the extent of one, two, or ten percent of the total liability. If so, it is possible that the award of $10,675,000 reflects the arbitrators application of a setoff in view of Merit's settlement with Lebowitz. The parties briefed these issues in full and supported their positions with oral argument. Certainly, the arbitrators could have made their decision on any one of those or other theories. *See, e.g., Sobel* v. *Hertz, Warner & Co., supra,* 469 F.2d at 1215.

This court must necessarily speculate whether the arbitrators "manifestly disregarded" the New Jersey contribution statute or whether in fact they found it applicable. As stated above, the extent of an arbitrator's obligation to explain his award is necessarily related to the scope of judicial review, and such review is severely limited where no reasons are given for the award. *Id.* at 1214. Furthermore, this court cannot properly reverse the award even if it was based upon a "clearly erroneous interpretation" of the New Jersey contribution statute. *See, e.g., I/S Stavborg* v. *National Metal Converters, Inc.,* 500 F.2d 424, 432 (2d Cir. 1974). No such showing is made here

Respondent as the challenging party has the burden to establish substantially more than an erroneous conclusion of law or fact. *Local Union No. 251* v. *Narragansett Improvement Co.*, 503 F.2d 309, 312 (1st Cir. 1974). Respondent has failed to sustain that burden.

V.

Respondent argues that the award should be vacated under §§10(b) and (c) of the Federal Arbitration Act because the arbitrators exhibited bias and prejudice towards LIC. At the outset, LIC claims that the arbitrators' decision to cut off any evidence of lost profits on June 30, 1979 prevented respondent from submitting subsequent data that would provide more accurate evidence of Merit's profitability. The argument, as respondent concedes, is similar to that of the "newly discovered evidence." (LIC Brief, pp. 54-55).

Respondent suggests that an accurate assessment of Merit's profitability for the years 1977 to 1979 could only be made in retrospect from financial statements that would become available in 1985. (See LIC Brief, pp. 53-55). In other words, an exact appraisal of Merit's lost profits for any stated period could only be made five years later. In effect, respondent suggests that the arbitrators were biased because they did not wait until 1985 to determine Merit's consequential damages with precision. This court does not agree.

Arbitration proceedings are not governed by the rules of evidence. *Shearson Hayden Stone, Inc.* v. *Liang*, 653 F.2d at 313. The arbitrators are vested with broad discretion and control over the procedures and standards used with respect to the evidence. It was certainly logical for the arbitrators to establish a cut off date for proof of

Merit's projected profitability; the alternative would have been to suspend the proceedings for several years in order to assess retrospectively Merit's actual profits. That approach is neither desirable nor practical. In addition, the cut off date of June 30, 1979 was sensible because it was the current date of the trial. (LIC Brief, p. 53). Certainly, it was reasonable for the arbitrators to consider all the financial statements that were available as of the time when the computation was to be made. Under respondent's suggestion, the arbitration would have been prolonged for several additional years in order to establish the company's future profitability with certainty, and any arbitration award could then be vacated because of any change in the company's financial status after the award has been made.

The respondent asserts that the arbitrators were prejudiced because they refused to hear evidence from Merit's independent auditors over the respondent's objection. Respondent concedes, however, that the auditors' refusal to testify in this matter on the ground of privilege was upheld by Judge Bua in *Western Employers Insurance Company* v. *Merit Insurance Company and Peat Marwick Mitchell & Co.*, 492 F. Supp. 53 (N.D. Ill. 1980). Respondent argues that the arbitrators were biased because they refused to compel the auditors to testify in spite of Judge Bua's ruling. (LIC Brief, pp. 56-57). That argument is misplaced. The arbitrators properly allowed the invocation of the auditors' privilege to be reviewed by this court, and they certainly exhibited no bias towards LIC by following the court's decision.

Respondent argues that the arbitrators manifested their bias by awarding Merit with $10,675,000, by issuing the clarification of their award in response to Merit's motion, and by one comment that an arbitrator made in May of

1979. This court has already noted that the amount of the award was not in manifest disregard of the applicable law, and that the sum of the award could have been supported by any one of several theories. Further, the arbitrators did nothing improper or irregular in issuing a clarification of their award in response to Merit's request. Finally, the entire context in which Mr. Bolton made his comment on page 7851 of the arbitration transcript indicates only that the arbitrator was expressing his opinion on the possible relevance of certain evidence that LIC had read into the record. Arbitrators are free to comment on the possible relevance of any evidence that comes before them.

In setting aside an award for bias, the Seventh Circuit Court of Appeals has stated the "guiding principle" is that "the interest or bias of an arbitrator must be direct, definite, and capable of demonstration rather than remote, uncertain, or speculative." *Tamari v. Bache Halsey Stuart Inc., supra,* 619 F.2d at 1200 citing *United States Wrestling Federation v. Wrestling Division of the AAU, Inc.,* 605 F.2d 313, 318 (7th Cir. 1979). That principle applies whether actual bias or merely an appearance of bias is charged. *Id.* at 1200. The arguments of respondent suggests at most that the possibility of bias was highly speculative, and there is no direct or definite indication in the record of such bias. At this stage of the proceedings, respondent's assertions that bias and prejudice characterized the arbitrators' conduct and award have a distinctly hollow ring.

VI.

Petitioner Merit asks this court to award interest in the event that judgment is entered on the arbitration award. As both parties correctly observe, state law governs the award of interest in diversity cases. *Michael-*

Regan Co., Inc., v. *Lindell,* 527 F.2d 653, 659 (9th Cir. 1975); *Lundgren* v. *Freeman,* 307 F.2d 104 (9th Cir. 1962). The parties dispute, however, whether the interest statute of Illinois, Ill. Rev. Stat., Ch. 74, §53, or of New Jersey, N.J.S.A.R. 4:42-11(a), should apply.

In cases such as this where the parties, arbitration, and transaction touch a number of states, the question may arise as to which state's law applies. *See, eg., In Re Air Crash Disaster Near Chicago, Ill., Etc.,* 480 F. Supp. 1280, 1282 (N.D. Ill. 1979) citing *Klaxon Co.* v. *Stentor Electric Mfg. Co., Inc.,* 313 U.S. 487, 496 (1941). This court finds, however, that it need not decide which state's law applies with respect to the issue of interest on the arbitration award. *Id.* at 1283. Only in cases where a conflict exists between the laws of the various states would it be necessary to decide the applicable state law. *Id.* at 1283. Where all of the states whose law might apply have substantially the same law, no conflict is presented. *Id.* at 1283. Because interest is available under the statutes of both Illinois and New Jersey, no true conflict of law therefore exists.

The applicable portion of the New Jersey statute provides:

> (a) RATE. Judgments, AWARDS and orders for the payment of money and taxed costs shall bear simple interest on the amount of the award at 8% per annum from the date of entry, except as otherwise ordered by the court. N.J.S.A.R. 4:42-11(a) (emphasis supplied)

A New Jersey court has construed the statute's applicability to an arbitration award by holding that interest should be computed from the date of the arbitration award. *Ukranian National Etc.* v. *J. L. Muscarelle, Inc.,* 151 N.J. Super. 386, 376 A.2d 1299 (1977). As a result,

interest would be computed on a per annum basis from the date of the arbitration award on December 1, 1980.

Similarly, Illinois' general interest statute provides in part:

> . . . [W]hen judgment is entered upon any AWARD, report or verdict, interest shall be computed at the above rate from the time when made or rendered to the time of rendering judgment upon the same, and made a part of the judgment. Ill. Rev. Stat., Ch. 74, §53 (emphasis supplied)

Illinois courts have held that interest should be computed from the date of the arbitration award and included into the judgment. *See, eg., Wrobel* v. *Argiris*, 73 Ill. App. 3d 648, 392 N.E.2d 681 (1979).

Interest on the arbitration award is therefore available under both the law of New Jersey and Illinois, and it should be computed on a per annum basis as of December 1, 1980, when the award was made. Because the parties agree that the law of New Jersey governed the arbitration, this court holds that the precise interest rate of 8% per annum applies to the award under the New Jersey statute.

VII.

For the foregoing reasons, the petition of Merit Insurance Company to confirm the arbitration award of $10,675,000, which was made on December 1, 1980, is granted. The motion of respondent Leatherby Insurance Company to vacate, to modify, or to correct the award is denied. The judgment confirming the award incorporates interest on the award as computed per annum from December 1, 1980 at the rate of 8%.

/s/ *Charles P. Kocoras*
Charles P. Kocoras
United States District Judge

DATED: November 19, 1981